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No. 91-14

Supreme Court, U.S.
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In the Supreme Court of the United States

OCTOBER TERM, 1991

NORTHERN NATURAL GAS COMPANY, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission reasonably concluded that, in the exercise of its power to establish just and reasonable rates "in connection with the transportation * * * of natural gas" in interstate commerce under Sections 4 and 5 of the Natural Gas Act (NGA), 15 U.S.C. 717c and 717d, the Commission may regulate rates that a natural-gas company charges for gathering gas for the purpose of transporting it interstate, notwithstanding the exclusion of the "gathering of natural gas" from the provisions of the NGA under Section 1(b), 15 U.S.C. 717(b).

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-29a) is reported at 929 F.2d 1261. The opinions of the Federal Energy Regulatory Commission are reported as follows: Order Approving Contested Offer of Settlement as Modified (Pet. App. 30a-32a), 37 F.E.R.C. ¶ 61,272; Order Granting in Part and Denying in Part Rehearing and Granting Clarification (Pet. App. 33a-35a), 41 F.E.R.C. ¶ 61,158; Letter Order (Pet. App. 38a-39a), 43 F.E.R.C. ¶ 61,158; Order Denying Appeal of Staff Action and Denying Rehearing (Pet. App. 40a-47a), 43 F.E.R.C. ¶ 61,473; and Order Denying Rehearing (Pet. App. 48a-56a), 44 F.E.R.C. ¶ 61,384. A Letter Order dated January 28, 1988, issued by the Commission's staff (Pet. App. 36a-37a), is unreported.

JURISDICTION

The judgment of the court of appeals was entered on April 4, 1991. The petition for a writ of certiorari was filed on July 2, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. Pursuant to the Natural Gas Act (NGA), ch. 556, 52 Stat. 821, 15 U.S.C. 717 *et seq.*, the Federal Energy Regulatory Commission (FERC) regulates the transportation of natural gas in interstate commerce, the sale in interstate commerce of natural gas for resale, and natural-gas companies.[1] Sections 4 and 5 of the NGA, 15 U.S.C. 717c and 717d, require FERC to establish "just and reasonable" rates "for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission."[2] 15 U.S.C. 717c(a). The jurisdiction of the Commission is described in Section 1(b) of the NGA, which states:

> The provisions of [the NGA] shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of

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[1] A "natural-gas company" is defined as a "person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." 15 U.S.C. 717a(6).

[2] These responsibilities were formerly exercised by FERC's predecessor, the Federal Power Commission (FPC), whose functions were transferred to FERC pursuant to the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. 565, and Exec. Order No. 12,009, 3 C.F.R. 142 (1978). References in this brief to FERC also include the FPC.

> natural gas for resale * * *, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

15 U.S.C. 717(b).

The "production or gathering of natural gas," excluded from the application of the NGA by Section 1(b), refers to "the physical acts of drawing the gas from the earth and preparing it for the first stages of distribution." *Northern Natural Gas Co.* v. *State Corp. Comm'n*, 372 U.S. 84, 89-90 (1963).[3] Traditionally, in setting the rate that a pipeline may charge for the jurisdictional sale of gas, FERC has included in the rate base all costs that underlie the sale, including the cost of gathering as performed by the pipeline. This Court has upheld FERC's authority to use that approach, rejecting the claim that it constitutes regulation of gathering in violation of Section 1(b). *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581, 600 (1945); *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954).

b. Prior to enactment of the Natural Gas Policy Act of 1978 (NGPA), Pub. L. No. 95-621, 92 Stat. 3350, 15 U.S.C. 3301 *et seq.*, interstate pipeline companies primarily operated as wholesalers of gas, selling the gas either to distributors for resale or to end-

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[3] As explained by the court of appeals, "gathering" is the process by which a producer, pipeline, or other company collects natural gas from wells at the point of production and moves it through a network of pipelines to a collection point for subsequent transportation through a pipeline's principal transmission system. Pet. App. 9a.

users. In those sales, gas and transportation were provided at a single "bundled" rate. Pet. App. 4a. The NGPA substantially loosened regulation of the wellhead prices of gas in order "to give market forces a more significant role in determining the supply, the demand, and the price of natural gas." *Transcontinental Gas Pipe Line Corp.* v. *State Oil & Gas Bd.*, 474 U.S. 409, 422 (1986) (*Transco*).[4] As a result, some customers of interstate pipelines began purchasing gas directly from producers or other sellers and then used the pipelines solely to transport the gas to them. See, *e.g.*, Pierce, *Reconsidering the Roles of Regulation and Competition in the Natural Gas Industry*, 97 Harv. L. Rev. 345, 348 (1983).

Partially in response to that trend, in 1985, FERC adopted Order No. 436,[5] which "envisage[d] a com-

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[4] Congress further implemented that policy through the Natural Gas Wellhead Decontrol Act of 1989, Pub. L. No. 101-60, 103 Stat. 157, which amended the NGPA and eliminated all wellhead price controls by January 1, 1993.

[5] Order No. 436, *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, 50 Fed. Reg. 42,408 (1985) (codified as amended in scattered sections of 18 C.F.R. Pts. 2, 157, 284, 375, 381), reh'g granted in part and denied in part, Order No. 436-A, 50 Fed. Reg. 52,217 (1985), reh'g granted in part, Order No. 436-B, 51 Fed. Reg. 6398 (1986), reh'g denied, Order No. 436-C, 51 Fed. Reg. 11,566 (1986), reh'g denied, Order No. 436-D, 51 Fed. Reg. 11,569 (1986), reconsideration denied, Order No. 436-E, 51 Fed. Reg. 11,566 (1986), vacated and remanded *sub nom. Associated Gas Distributors* v. *FERC*, 824 F.2d 981 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988), readopted on an interim basis on remand, Order No. 500, 52 Fed. Reg. 30,334 (1987), extension granted, Order No. 500-A, 52 Fed. Reg. 39,507 (1987), modified, Order No. 500-B, 52 Fed. Reg. 39,630 (1987), modified further, Order No. 500-C, 52 Fed. Reg. 48,986 (1987), modified further, Order No. 500-D, 53 Fed. Reg. 8439 (1988), reh'g denied, Order No. 500-E, 53 Fed. Reg. 16,859 (1988),

plete restructuring of the natural gas industry." *Associated Gas Distributors* v. *FERC*, 824 F.2d 981, 993 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988). In order No. 436, the Commission instituted a program to encourage open access to all major pipelines, so that local distributing companies and other pipeline customers could purchase gas directly from producers. The Commission found that the pipelines' practice of refusing to transport gas in competition with their own sales was unduly discriminatory because it denied consumers access to gas at the lowest reasonable prices. The Commission also found that the practice was frustrating the NGPA's goal of relying on a competitive wellhead market in reducing prices. See Pet. App. 4a-5a.

To encourage the competitive benefits of having pipelines transport natural gas that customers had purchased from others, Order No. 436 allowed a pipeline to obtain a "blanket certificate" of public convenience and necessity under Section 7(c) of the NGA, 15 U.S.C. 717f(c), authorizing the pipeline to transport natural gas without obtaining prior Commision approval of each transportation arrangement. FERC noted that the NGPA had left a "generally competitive market" for natural gas and had made gas "a separate and distinct economic *commodity*," separate from transportation and other services provided by pipelines. 50 Fed. Reg. 42,412,

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modified further, Order No. 500-F, 53 Fed. Reg. 50,924 (1988), reh'g denied, Order No. 500-G, 54 Fed. Reg. 7400 (1989), remanded, *American Gas Ass'n* v. *FERC*, 888 F.2d 136 (D.C. Cir. 1989), readopted, Order No. 500-H, 54 Fed. Reg. 52,344 (1989), modified, Order No. 500-I, 55 Fed. Reg. 6605 (1990), aff'd in part and remanded in part, *American Gas Ass'n* v. *FERC*, 912 F.2d 1496 (D.C. Cir. 1990), cert. denied, 111 S. Ct. 957 (1991), stayed in part on remand, Order No. 500-J, 56 Fed. Reg. 6992 (1991).

42,413 (1985). But in many geographic markets, pipelines remained monopoly providers of transportation service. Therefore, if a pipeline offered transportation service under a blanket certificate, Order No. 436 requires it to provide transportation service without undue discrimination or preference. 18 C.F.R. 284.8(b). See 50 Fed. Reg. 41,421, 42,424-42,425, 42,430 (1985).

2. a. Petitioner Northern Natural Gas Company (Northern) is an interstate pipeline company regulated as a natural-gas company under the NGA. In 1985, Northern filed a proposed rate tariff for open-access transportation. The tariff did not set forth rates for gathering provided in connection with that transportation, as required by Order No. 436. In response to objections by FERC's trial staff and several of Northern's customers, Northern replied that it would charge for gathering separately and urged that Section 1(b) of the NGA did not give the Commission jurisdiction to require that a gathering rate be filed. In approving a contested offer of settlement, the Commission required Northern to reflect its gathering rates in its tariff sheets. Pet. App. 30a-32a. The Commission noted that Order No. 436 requires an open-access transportation tariff to "separately identify cost components attributable to transportation, storage, and gathering costs," 18 C.F.R. 284.7 (d)(1), and that if Northern were required to state its rates for gathering in its transportation tariff, "potential shippers will be apprised of the full cost of the services they intend to purchase." Pet. App. 32a, 33a-35a.

Northern then filed a tariff sheet setting forth gathering rates, but with a footnote declaring that those rates were "[p]rovided for informational pur-

poses only and not as a limitation of prices which may be charged or to imply recognition of or assent to Commission jurisdiction over such activities." Pet. App. 57a. The Commission's staff rejected that filing because the gathering rates were not derived from gathering costs and, by virtue of the footnote, were not "stated rates" binding on Northern. *Id.* at 36a-37a. Northern appealed this order to the Commission but filed a new tariff sheet omitting the footnote, *id.* at 58a, which the Commission accepted for filing as complying with its orders. *Id.* at 38a-39a.

b. The Commission denied Northern's appeal of the order rejecting the footnoted tariff sheet and its request for rehearing of the order accepting the tariff sheet without the footnote. Pet. App. 40a-47a. FERC concluded that "Congress's grant to the Commission of jurisdiction over the rates * * * for services ancillary to the transportation and sale of natural gas in interstate commerce includes the authority to determine the justness and reasonableness of the rates * * * of Northern's gathering services here at issue." *Id.* at 44a.[6]

The Commission explained that its power to determine the justness and reasonableness of the rates for Northern's gathering service derives from Sections 4(a) and 5(a) of the NGA, 15 U.S.C. 717c(a), 717d(a). Pet. App. 42a. Those provisions, the Commission observed, authorize it to regulate not only the rates charged "for" the transportation or sale of gas within its jurisdiction, but also the rates charged "in connection with" such transportation or sale. *Id.* at 43a. The Commission concluded that "the gather-

[6] The Commission thus found it unnecessary to determine whether Northern's service was, in fact, "gathering" within the meaning of Section 1(b) of the NGA. Pet. App. 42a, 44a.

ing here at issue is provided in connection with Northern's open-access transportation" under Order No. 436, and is therefore subject to FERC regulation. Pet. App. 44a-45a. The Commission also pointed out that if it did not have jurisdiction over the rates for gathering, "there would be a gap in the regulation of gas in interstate commerce, contrary to Congress's intent." *Id.* at 44a. Reiterating the findings it made in Order No. 436, the Commission further stated that "excessive rates for gathering services provided in connection with open-access transportation could be used as a barrier to open-access transportation and would also defeat the goal of lower prices to consumers." *Id.* at 45a.[7]

In denying rehearing, the Commission again rejected Northern's contention that Section 1(b) excludes Northern's gathering rates from its jurisdiction. Pet. App. 48a-56a. The Commission stated that Northern's argument "ignores the distinction drawn between state jurisdiction over the physical activity of gathering and federal jurisdiction over the rates charged for gathering provided in connection with jurisdictional sales and transportation." *Id.* at 55a. The Commission responded to Northern's contention that it had not previously regulated gathering rates

[7] The Commission took note of Northern's reliance on the Section 1(b) gathering exemption, but found that "[a]t most," that Section would "exempt Northern's gathering service and facilities from NGA Section 7 certificate jurisdiction." Pet. App. 42a. The Commission explained that this Court had construed the gathering exemption "to apply to non-price matters such as the 'physical activities, facilities, and properties used in the . . . gathering of natural gas.' " *Id.* at 46a (quoting *Interstate Natural Gas Co.* v. *FPC*, 331 U.S. 682, 690 (1947)). The exemption, therefore, did not apply to price regulation under Sections 4 and 5. Pet. App. 46a-47a.

by noting that pipelines had in the past "served primarily as merchants of natural gas" and "[t]he cost of gathering was rolled into the interstate pipelines' sales for resale rates." Accordingly, "there was no need to give special scrutiny to gathering rates or service apart from regulation of the sales rates." *Ibid.* But because pipelines had since become primarily transporters of natural gas, the Commission explained, it "must now separately scrutinize the rates charged for gathering performed in connection with transportation in order to insure that the Commission's policies underlying open-access transportation remain intact." *Id.* at 55a-56a.

3. The court of appeals upheld the Commission's orders, determining that the Commission has authority under Sections 4 and 5 of the NGA to regulate the rates Northern charges for gathering performed through its own facilities in connection with transportation in interstate commerce. Pet. App. 1a-29a.

The court of appeals found the circumstances in this case to be "nearly identical" to those in *Colorado Interstate Gas Co.* v. *FPC*, *supra*. Pet. App. 27a. There, the court noted, this Court sustained "the regulation of rates for gathering performed in connection with interstate sales," notwithstanding the exclusion of gathering from FERC's jurisdiction in Section 1(b) of the NGA. Pet. App. 18a. Given that ruling, "it would be inconsistent to hold that the Commission may not regulate rates for transportation over a pipeline's own gathering facilities performed in connection with admittedly jurisdictional interstate transportation." *Ibid.* The court explained that if a pipeline could set an unregulated rate for such gathering, it could effectively establish its own rates for interstate transportation. That result

would allow the pipeline to prefer its gas sales over the transportation of gas for others, thereby thwarting the procompetitive purposes of Order No. 436, the NGA, and the NGPA. Pet. App. 19a, 20a.

The court also found no justification in Section 1(b)'s gathering exemption for setting aside the Commission's orders in this case. That exemption, the court explained, is "confined * * * to matters of state and local concern" involving the physical acts of drawing gas from the ground and channeling it for initial distribution. Pet. App. 21a-22a. Nor did the court find that *Colorado Interstate*'s reading of Section 1(b) was undercut by any of this Court's later decisions interpreting the gathering exemption. Pet. App. 21a-24a. Finally, the court concluded that its holding does not conflict with the Tenth Circuit's decision in *Northwest Pipeline Corp.* v. *FERC*, 905 F.2d 1403 (1990), because that case involved a different issue—whether certain pipeline facilities were "gathering" or "transportation" facilities. Pet. App. 25a-26a. The court noted that the Tenth Circuit had remanded for further consideration of that issue, while "[d]eclining to address" whether the Commission has authority under Sections 4 and 5 of the NGA to regulate a pipeline's gathering rates in connection with its interstate transportation. Pet. App. 25a-26a.[8]

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[8] The court also rejected Northern's contention that the Commission's regulation of Northern's gathering rates in connection with its interstate transportation constituted "discriminatory treatment," inasmuch as gathering performed by producers or independent gatherers was not similarly regulated. Pet. App. 27a. The court pointed out that because no producers or independent gatherers were before the court, it did not have to determine whether they were subject to regulation under Sections 4 and 5. Pet. App. 27a. Moreover, the

ARGUMENT

The court of appeals correctly held that the Commission, in regulating the transportation of natural gas in interstate commerce, has the authority to regulate the rates charged by a pipeline for gathering natural gas in connection with that transportation. The holding follows logically from this Court's decision in *Colorado Interstate* and is fully consistent with the statutory framework of the NGA and this Court's interpretation of the NGA's gathering exemption. Contrary to petitioner's contention, the court of appeals' decision does not conflict with any decision of this Court or of any other court of appeals. Review therefore is not warranted.

1. Petitioner contends (Pet. 4-16) that the gathering exemption in Section 1(b) provides complete immunity from FERC regulation of its gathering rates under Sections 4 and 5 of the NGA, even though petitioner's gathering is performed over its own lines in connection with interstate transportation and the Commission is regulating neither gathering facilities nor the physical activity of gathering. That contention is based on a misreading both of the applicable provisions of the NGA and of this Court's holding in *Colorado Interstate.*

a. FERC's jurisdiction in this case is grounded in the fact that petitioner's gathering rates are integrally tied to its transportation of gas in interstate commerce. Section 4(a) of the NGA provides:

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court noted, the Commission had explained that producers are regulated under separate provisions, and independent gatherers do not have the same power to engage in anticompetitive abuses as pipelines performing both transportation and gathering. *Id.* at 28a.

> All rates and charges made, demanded, or received by any natural-gas company for *or in connection with* the transportation or sale of natural gas subject to the jurisdiction of the Commission * * * shall be just and reasonable.

15 U.S.C. 717c(a) (emphasis added). Section 5(a) provides that the Commission may determine and prescribe the "just and reasonable rate" whenever it finds that

> any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company *in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission* * * * is unjust, unreasonable, unduly discriminatory, or preferential.

15 U.S.C. 717d(a) (emphasis added). Petitioner's gathering rates come within the reach of these provisions because they are set "in connection with" natural-gas transportation that is unquestionably within the Commission's jurisdiction to regulate under Section 1(b). See 15 U.S.C. 717(b) (NGA applies to "transportation of natural gas in interstate commerce"). The power to regulate rates "in connection with" jurisdictional transportation supplements FERC's power to regulate rates "for" such transportation. 15 U.S.C. 717c(a). As the court of appeals explained, petitioner's gathering services are rendered as part of a continuous flow of gas over its own facilities, and the gathering is required to accomplish a single act of transportation of gas in interstate commerce. Pet. App. 25a. Regulation of gathering rates is not only justified by the NGA, it is "essential to prevent discrimination against third-party gas in interstate transportation and sales." *Ibid.* See 15 U.S.C. 717d(a) (prohibiting unduly discriminatory or preferential rates).

The "gathering" exemption in Section 1(b) does not preclude FERC's jurisdiction over rates under Sections 4 and 5. In relying on the "express language" of Section 1(b), Pet. 4-6, petitioner ignores the fact that, in keeping with the recognition that "[e]xceptions to the primary grant of jurisdiction * * * are to be strictly construed," *Interstate Natural Gas Co.* v. *FPC*, 331 U.S. 682, 690-691 (1947), this Court "has consistently held that 'production' and 'gathering' are terms narrowly confined to the physical acts of drawing the gas from the earth and preparing it for the first stages of distribution." *Transco*, 474 U.S. at 418 (quoting *Northern Natural Gas*, 372 U.S. at 90). See *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 678 (1954) ("exemption applies to the physical activities, facilities, and properties used in the production and gathering of natural gas"); *Interstate Natural Gas*, 331 U.S. at 690 (gathering exemption "reserve[s] to the States * * * the power to regulate the physical production and gathering of natural gas in the interests of conservation or of any other consideration of legitimate local concern"); *Colorado Interstate*, 324 U.S. at 602-603 (exemption applies to "activity of producing or gathering natural gas"). The Commission is not regulating the physical activities or facilities of gathering in this case, nor is it trenching on an area of local concern. Rather, the Commission is regulating gathering rates when a pipeline gathers gas in connection with its interstate transportation. No decision of this Court holds that such regulation runs afoul of the gathering exemption. Indeed, this Court's decision in *Colorado Interstate*, by allowing the Commission to set the amount of gathering costs to be included in the rate base for jurisdictional sales, firmly establishes that the Commission's regulation of petitioner's gath-

ering rates is consistent with the gathering exemption.[9]

Thus, the Commission's regulation of the gathering rates at issue here is clearly authorized by the NGA. Even if the provisions of the NGA were more ambiguous on the point, the Commission's interpretation of Sections 1(b), 4, and 5 to apply to petitioner's gathering is reasonable and is entitled to deference under *Chevron U.S.A. Inc.* v. *Natural Resources De-*

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[9] Petitioner suggests in passing (Pet. 6-7) that the legislative history suports its broad view of the gathering exemption, but cites only cases discussing Congress's general intention to preserve state regulation over gathering. The traditional domain of state regulation, however, does not extend to dictating the rate-of-return on gathering services performed in connection with jurisdictional sales or transportation. See pp. 18-20, *infra*. The Interstate Natural Gas Association of America (INGAA) does canvass the legislative history (Br. 5-7), but fails to mention that this same material was before the Court in *Colorado Interstate*. There, the Court was not persuaded that Congress intended to prevent the Commission from determining the costs allocable to gathering when it established a rate-base for interstate sales; the dissent took a contrary view of the legislative history. See 324 U.S. at 599-600; *id.* at 621, 623 (Stone, C.J., dissenting). There is no reason for the Court to revisit that dispute. Cf. *California* v. *FERC*, 110 S. Ct. 2024, 2033 (1990). In any event, the statement by FPC Solicitor DeVane, cited by INGAA (Br. 6), that the Commission would not have jurisdiction over "gathering rates" was not addressed to the situation that the Commission confronted here of an integrated pipeline-gatherer establishing putatively separate rates for what is in reality a single act of interstate transportation. Indeed, DeVane recognized that the Commission, in regulating a pipeline's sales rates, would *not* be bound by the gathering price paid by a pipeline "if the transaction was not at arm's length." *Natural Gas: Hearing on H.R. 11662 Before a Subcomm. of the House Comm. on Interstate and Foreign Commerce*, 74th Cong., 2d Sess. 42-43 (1936).

fense Council, Inc., 467 U.S. 837, 842-845 (1984). See *Mobil Oil Exploration & Producing Southeast, Inc.* v. *United Distribution Cos.*, 111 S. Ct. 615, 624 n.5 (1991).

b. The conclusion that the Commission has authority over petitioner's gathering rates here is also compelled by *Colorado Interstate*. In that case, the Court held that Section 1(b) "does not preclude the Commission from reflecting the production and gathering facilities of a natural gas company in the rate base and determining expenses incident thereto for the purposes of determining the reasonableness of rates subject to its jurisdiction." 324 U.S. at 603. As a matter of substance, the Commission is doing nothing more here by regulating the gathering rates that petitioner offers to customers purchasing petitioner's interstate transportation services, where the transaction requires that the gas be moved through petitioner's own gathering facilities.

The companies in *Colorado Interstate* sold gas for resale in interstate commerce; one of them (Canadian) also produced and gathered the gas. 324 U.S. at 585. Claiming that the Commission was improperly "regulat[ing] the production and gathering of natural gas," contrary to Section 1(b), Canadian objected to the inclusion of its production and gathering costs in the rate base used to determine its interstate-sales rates. 324 U.S. at 597. Canadian insisted that the proper approach was for the Commission to accept, as one of Canadian's operating expenses, the "fair field price" or "fair market value" of the gas that was gathered and channeled into "the transmission lines for interstate transportation and sale." *Id.* at 600.[10] This Court held that because the

[10] The dispute effectively concerned the rate that Canadian could charge for its gathering operations as used in inter-

gathering charge was reflected in the ultimate price paid by the purchaser in a transaction that the Commission had jurisdiction to regulate, the Commission also had authority to determine what value could be assigned in the rate base to gathering facilities and expenses. *Id.* at 600, 603. The Court rejected the contention that the gathering exemption precluded that approach, stating that Section 1(b) "must be reconciled with the explicit provisions [of the NGA] which describe the normal conventions of rate-making." 324 U.S. at 602.

The rationale of *Colorado Interstate* governs this case. As the court of appeals explained, "[f]or the Commission to regulate separately stated rates for gathering over the pipeline's own gathering lines performed *in connection with* further jurisdictional interstate transportation is the substantial equivalent of the control of rates for gathering upheld in *Colorado Interstate*." Pet. App. 17a-18a. Petitioner's effort to distinguish *Colorado Interstate* relies on an artificially narrow reading of the decision. Petitioner points out that its gathering rate is stated separately from its transportation rate; in petitioner's view (Pet. 14), "[t]he critical consideration in *Colorado Interstate* is the fact that the jurisdictional sales rate at issue therein *included* both the cost of jurisdictional transportation and an allocation of the costs of nonjurisdictional production and gathering." But, as the court of appeals explained, petitioner's statement of separate rates for gathering

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state sales. The Commission allowed Canadian a 6 1/2 percent return on its rate base; the inclusion of gathering *costs* rather than *market value* substantially reduced Canadian's rate of return on its gathering operations. See 324 U.S. at 588, 597.

and transportation does not alter the fact that petitioner is offering a single, integrated service:

> It is insignificant that transportation rather than sale is the service involved [in this case] or that the rate for gathering is to be stated separately rather than "bundled." Stating the gathering rate separately from the related jurisdictional transportation rate does not magically "unbundle" the actual gathering activity performed over the pipeline's own facilities in connection with continuing interstate transportation.

Pet. App. 27a.[11]

In *Colorado Interstate* the pipeline's interstate *sale* of natural gas represented a bundle of goods and services (the production and gathering of the gas, plus transportation to the purchaser); here, the Commission determined that petitioners' interstate *transportation* of natural gas likewise represents a bundle of services, albeit with different components (the

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[11] Petitioner quotes out of context (Pet. 12) the statement in *Colorado Interstate* that "the authority of the Commission to suspend rates is restricted to rates over which it has jurisdiction." 324 U.S. at 596. The point of that statement was that a proviso in Section 4(e) of the NGA that barred the Commission from suspending the rate for "gas sold for resale for industrial use" confirmed that such sales were within the Commission's jurisdiction; otherwise, "the proviso in § 4(e) would be unnecessary." 324 U.S. at 596. The Court did not state that gathering rates that are integral to interstate transportation or sale are beyond the Commission's regulatory jurisdiction. Moreover, when the Court did turn to the gathering exemption, it held that the Commission could establish the cost of gathered gas—and thereby effectively determine its "rate"—in the rate base for a jurisdictional sale. *Id.* at 601.

gathering of the gas plus transportation to the purchaser). In each case, the Commission has the power to regulate the *total* price of the bundle of products and services; the pipeline is not free to escape that regulation by unbundling one integrally related service and then charging whatever the market will bear. To hold otherwise would "permit the *pipeline* to establish rates for the interstate transportation." Pet. App. 19a. Just as Section 1(b) did not shield gathering from regulation in *Colorado Interstate*, it cannot shield petitioner's gathering from regulation in this case.

c. Petitioner errs in contending (Pet. 7-9) that the decision below conflicts with *FPC* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498 (1949). In *Panhandle Eastern*, the Court held that the production and gathering exemption includes "facilities" as well as "activities," and thereby prevents the Commission from barring an interstate pipeline from selling part of its undeveloped gas reserves. *Id.* at 504-505. Here, by contrast, FERC has not exerted control over the "facilities" of gathering; it has regulated rates for gathering undertaken in connection with jurisdictional transportation.[12] *Panhandle East-*

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[12] Petitioner cannot obtain the protection of the gathering exemption simply because its gathering facilities are "affected" by rate regulation. See Pet. 9-10. In *Colorado Interstate*, the Court rejected the same argument when it acknowledged that the Commission's consideration of the costs of "producing properties and gathering facilities has of course an indirect effect on them." 324 U.S. at 603. As the Court later observed in *Interstate Natural Gas Co.* v. *FPC*, 331 U.S. 682, 691 (1947), "[i]t is not sufficient to defeat the Commission's jurisdiction over sales for resale in interstate commerce to assert that in the exercise of the power of rate regulation in such cases, local interests may in some degree be affected."

ern specifically recognized that the Commission's use of production and gathering cost data to fix rates does not violate the gathering exemption. *Id.* at 506 (citing *Colorado Interstate*, 324 U.S. at 602).[13]

Nor does the court of appeals' decision conflict with this Court's cases construing Section 1(b) to reserve a zone of regulatory authority to the States. See Pet. 11-12. In *Northwest Central Pipeline Corp.* v. *State Corp. Comm'n*, 489 U.S. 493, 511 (1989), the Court held that Section 1(b) allows a State to regulate the "proration of gas production in aid of conservation and the protection of correlative rights." The Court, however, did not hold that the financial return from gathering provided as a component of interstate transportation is subject only to state regulation; to the contrary, the Court reaffirmed that the production-and-gathering exemption relates to "the physical acts of drawing gas from the earth and preparing it for the first stages of distribution." *Id.* at 510.

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[13] It is not anomalous, as petitioner contends (Pet. 9), that this interpretation of *Panhandle Eastern* produces something of a "split" application of the NGA, under which FERC has jurisdiction over certain gathering rates under Sections 4 and 5 of the NGA, where integrally related to the interstate transportation or sale of gas, but has no certification or abandonment jurisdiction over the gathering facilities and services themselves under Section 7, 15 U.S.C. 717f. That result is consistent with this Court's view that Section 1(b) removes only the "*physical* activities, facilities, and properties used in production and gathering" from the Commission's jurisdiction. *Phillips Petroleum*, 347 U.S. at 678 (emphasis added). Moreover, it is well settled that a finding that FERC has rate jurisdiction over an activity does not require that the Commission have certificate jurisdiction. *Mid-America Pipeline Co.* v. *FPC*, 330 F.2d 226, 228-229 (D.C. Cir. 1964); Pet. App. 47a n.20.

Moreover, where, as here, a pipeline company effectively bundles gathering service with interstate transportation or sales for resale, state regulation of the gathering service is impracticable.[14] See *Phillips Petroleum*, 347 U.S. at 682-685; *Interstate Natural Gas*, 331 U.S. at 692-693. To our knowledge no state regulatory body has asserted jurisdiction over the gathering rates at issue here, and petitioner does not contend that FERC regulation is inconsistent with state law. See *Interstate Natural Gas*, 331 U.S. at 691-692. Indeed, state regulation of petitioner's rates for services so integrally related to interstate transportation of gas would enter the field of rate regulation reserved to FERC. Cf. *Schneidewind* v. *ANR Pipeline Co.*, 485 U.S. 293, 308 (1988).

d. Finally, petitioner claims (Pet. 4, 16) that FERC has departed from its traditional practice in asserting jurisdiction over gathering rates. See also INGAA Br. 15-16. That claim is a red herring. As the Commission explained, "[t]he issue of the Commission's authority to regulate the rates, terms, and conditions of gathering performed by pipelines on behalf of others has not previously arisen, because until recently pipelines generally did not perform such service" and "[t]here was therefore no need to give special scrutiny to gathering rates or services apart from regulation of the sale rates." Pet. App. 45a n.15. In regulating interstate sales, however, the Commission *has* long engaged in the equivalent of regulating gathering rates by setting the costs that

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[14] The impracticality of state regulation is illustrated by an exhibit to one of Northern's gathering contracts, which shows that Northern will provide gathering from two wells in Oklahoma to delivery points in Texas. Pet. App. 59a.

pipelines may include in their rate base.[15] By asserting authority over the rates for gathering provided as an integral part of interstate transportation, FERC is applying firmly established jurisdictional principles to current industry conditions.

2. Contrary to petitioner's contention (Pet. 16-24), the decision below does not conflict with the decision of any other court of appeals. In *Northwest Pipeline Corp* v. *FERC*, 905 F.2d 1403 (1990), the Tenth Circuit held that the Commission had applied an incorrect standard in determining that certain pipeline facilities were used for transportation rather than gathering.[16] The Tenth Circuit explicitly declined to decide the issue that was dispositive in this case, stating that "[u]ntil FERC resolves this ques-

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[15] As *Colorado Interstate* illustrates, FERC does not simply accept the market price for production and gathering, but rather sets a cost-based rate that allows the pipeline to recover its operating costs and a return on its investment. The wholesale purchaser pays a single FERC-regulated sales rate, not a FERC-regulated transportation rate plus an unregulated production and gathering rate. Thus, if the pipeline sells gas it has produced and gathered, the FERC-regulated sales rate comprehends a regulated rate for production and gathering. This approach has been followed by FERC for decades—with respect to petitioner's sales rates as well as others. See, *e.g.*, *Northern Natural Gas Co.*, 12 F.P.C. 66, 70-83 (1953) (Buchanan, Chairman, dissenting); *Northern Natural Gas Co.*, 11 F.P.C. 174, 200-208 (Smith, Comm'r, concurring), modified, 11 F.P.C. 400 (1952); *Northern Natural Gas Co.*, 11 F.P.C. 123, 150-153 (Smith, Comm'r, concurring), reh'g denied, 11 F.P.C. 375 (1952), aff'd *sub nom. State Corp. Comm'n* v. *FPC*, 206 F.2d 690 (8th Cir. 1953), cert. denied, 346 U.S. 922 (1954).

[16] FERC did not reach that issue here, but assumed for purposes of its decision that petitioner's services were actually "gathering" within the meaning of Section 1(b). Pet. App. 42a, 44a.

tion [whether the facilities were gathering or transportation facilities], we do not consider its alternate argument that sections 4(a) and 5 of the NGA * * * provide another mechanism for asserting jurisdiction to review the rates charged." 905 F.2d at 1411 n.23. As the court of appeals noted in this case, "[t]here is no conflict between [the Tenth Circuit's] opinion and the theory of our decision. We determine precisely the issue that [the Tenth Circuit] declined to decide." Pet. App. 26a.[17]

Nor is petitioner correct in contending (Pet. 19-23) that the court of appeals' decision conflicts with *American Gas Ass'n* v. *FERC*, 912 F.2d 1496 (D.C. Cir. 1990), cert. denied, 111 S. Ct. 957 (1991). That case upheld FERC's refusal to claim jurisdiction under Section 5 of the NGA to modify the non-price terms of "take-or-pay" clauses in nonjurisdictional contracts betweeen producers and pipelines. 912 F.2d at 1505-1507.[18] The court rejected the contention that Section 5 of the NGA provides jurisdiction over

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[17] Both petitioner and INGAA attribute the Tenth Circuit's statement in *Northwest Pipeline* that the Commission does not have "express or implied rate-regulatory jurisdiction of the production and gathering of gas" to a quotation from this Court's opinion in *Colorado Interstate*. Pet. 17, 18; INGAA Br. 18-19. As is clear from the Tenth Circuit's opinion, 905 F.2d at 1406, however, the quoted language is from the court of appeals' opinion in *Colorado Interstate* v. *FPC*, 142 F.2d 943, 952 (10th Cir. 1944), aff'd, 324 U.S. 581 (1945). In any event, the quoted statement did not purport to address the issue presented in this case, which the Tenth Circuit expressly reserved.

[18] "A take-or-pay clause requires a purchasing pipeline to take a specified volume of gas from a producer, or, if it is unable to do so, to pay for the specified volume." *Mobil Oil*, 111 S. Ct. at 622 n.3.

"any contract that would likely influence a pipeline's end-of-the-pipeline charges." *Id.* at 1505. The court of appeals did not uphold such an attenuated theory of jurisdiction in this case. Rather, its decision was "narrowly confined to rates for gathering by an interstate pipeline over its own lines in connection with jurisdictional interstate transportation." Pet. App. 22a.

Even farther afield are *Mobil Oil Corp.* v. *FPC*, 463 F.2d 256 (D.C. Cir. 1971), cert. denied, 406 U.S. 976 (1972), and *Pennzoil Co.* v. *FERC*, 645 F.2d 360 (5th Cir. 1981). See Pet. 22-23. In the former, the court held that the Commission had no jurisdiction under the NGA to regulate payments made by natural-gas producers to landowners. The court found that the landowners, in entering into leases with producers that called for royalty payments, were not sellers of gas for resale in interstate commerce because the transactions were "too far removed from the interstate sale." 463 F.2d at 258, 263. Here, of course, petitioner's gathering service is integral to its interstate transportation of gas and constitutes but one component of a single transaction. In *Pennzoil*, the court held that FERC had no jurisdiction over price-escalation clauses in contracts removed from NGA jurisdiction. 645 F.2d at 380-382. No issue was presented with respect to FERC's jurisdiction to regulate gathering rates "in connection with" jurisdictional sales.

3. Finally, petitioner argues (Pet. App. 24-26) that the Commission is impermissibly asserting "selective" jurisdiction by regulating the rates for gathering performed by pipelines in connection with interstate transportation, but not regulating the rates for gathering performed by non-pipelines (such as producers or independent gathering companies).

The Commission, however, explained that the potential for anticompetitive abuse in the instant context is not present in the other situations noted by petitioner. Pet. App. 44a. As the court of appeals pointed out, *id.* at 28a, independent producers or gatherers do not possess monopoly power over transportation facilities; thus, the Commission's refusal to assert jurisdiction over the gathering rates they charge is consistent with the NGA and the Commission's Order No. 436. Although petitioner asserts (Pet. 26 n.8, 27 n.10) that its gathering rates are established by a competitive market, the record in this case provides no support for that contention. This case, therefore, does not present the question whether the existence of competition in gathering markets is relevant to the Commission's authority to set gathering rates under the NGA.[19]

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[19] Petitioner also briefly contends (Pet. 27-28) that FERC cannot regulate the gathering activities of separately incorporated affiliates of a pipeline. That issue, however, is not presented in this case. Neither the Commission's orders nor the opinion below discuss the issue, and no record was developed concerning the extent of petitioner's control over its affiliates' gathering facilities. Petitioner concedes (Pet. 2) that it is an interstate pipeline and does not contend that it has any affiliates that are not themselves "natural-gas companies" subject to NGA regulation but that are adversely affected by the orders under review. Accordingly, the application of the decision below to a separately incorporated affiliate does not warrant review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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